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Syria: The State of the Economy

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Intelligence Memorandum

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Syria: The State of the Economy

KEY JUDGMENTS

After years of uncertain and haphazard development, Syria at last appears to be on the path of sustained economic growth. GDP, which has risen at an average annual rate of 9% since the Assad regime took over in 1969, jumped 12% last year and continues strong.

Unprecedented financial aid – chiefly from oil-rich Arab nations, the USSR, and the East European countries, but including significant development capital from Western sources – is fueling an ambitious program of economic expansion. The completion of the first stage of the Euphrates dam complex – the most important Syrian project – will double electrical power capacity and open vast new lands to agricultural development this fall.

Expanding export sales of petroleum and, to a lesser extent, phosphates and agricultural commodities will continue to play an important role in Syria's economic expansion.

While improvements in the Middle East political climate would enhance economic development prospects, Syria should be able to maintain its current pace of development in a no-war/no-peace environment.

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Note: Comments and queries regarding this memorandum are welcomed. They may be directed to [REDACTED] the Office of Economic Research, Code 143, Extension 7931.

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DISCUSSION

Background

1. Syria's present economic stability contrasts sharply with its turbulent past. During the late 1950s and most of the 1960s, agrarian reform and nationalization of key economic sectors - including industry, banking, and foreign trade - disrupted the Syrian economy. These developments combined with political turmoil to limit economic growth. The real annual growth rate for the period 1963-69 never exceeded 6%.
2. The economic situation improved sharply after the Assad regime took power in March 1969. Aided by political stability and more rational and balanced economic policies, gross domestic product (GDP) rose an average of 9% a year in real terms from 1969 through 1972. Syria's GDP reached US \$1.5 billion or about \$225 per capita in the latter year. Growing petroleum and phosphate output led to the expansion. Government investment in infrastructure and industry as well as government moves to stimulate private investment, to attract Arab development funds, and to liberalize exchange and trade controls also served to spur the economy.
3. The October war combined with severe drought halted real growth in 1973. Electrical power generation facilities and petroleum refining and storage areas were especially hard hit by Israeli air attacks.

1974 in Perspective

4. Massive infusions of Arab aid fueled restoration of Syria's war-shattered economy in 1974. A bumper agricultural year, along with increased investment in the industrial sectors, resulted in a growth rate of about 12% in real terms. The last three months of 1974 witnessed a dramatic increase in capital equipment imports. Industrial projects for which contracts had either been signed or were in the pipeline totaled nearly \$1.5 billion by yearend. With repair on most war-damaged facilities nearing completion and new industrial projects coming on stream, Damascus was clearly attempting to lay the foundations for sustained economic development.

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Balance-of-Payments Overview

5. Large aid receipts from Arab oil producers together with increased revenues from petroleum and agricultural commodities have kept the balance of payments in overall surplus since 1971. Reserves rose gradually from a low of \$55 million at the end of 1970 to \$244 million in September 1973 after which they jumped, reaching \$1.1 billion in May 1975.

Short-Term Outlook for 1975

6. Barring a new war, the Syrian economy should finish 1975 in a strong position (see the table). Syria's foreign payments balance should continue to improve; a surplus of \$600 million is projected. Although slow world economic recovery may cause some slippage in projected export earnings, the large increase in capital and aid receipts will more than balance any export deficiency. By the end of 1975, reserves should be at least \$1.4 billion, equivalent to almost one year's imports.

Syria: Balance-of-Payments Summary

	Million US \$	
	1974	1975
Exports	695	905
Imports ¹	1,070	1,550
Trade balance	-375	-645
Net services and private transfers	234	235
Current account balance	-141	-410
Grant-type assistance	445	730
Other capital inflows	50	281
Capital account balance	495	1,011
Balance to reserves	354	601

1. Excluding most military imports.

Exports

7. Commodity export earnings are expected to exceed the 1974 level by 30%. Crude oil, cotton, and phosphate rock, over 95% of total exports, will provide all of this increase, as shown in the following tabulation:

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8. Crude oil exports, now fully recovered from the effects of the war, will remain the single most important foreign exchange earner. About two-thirds of projected export receipts will be generated by oil sales. Government oil officials predict that production will exceed 200,000 b/d. We anticipate, however, that domestic consumption requirements will limit export sales to no more than 175,000 b/d.

	<u>Million US \$</u>	
	1974	1975
Total	695	905
Crude oil	400	575
Agricultural commodities	250	270
Phosphate rock	35	50
Other	10	10

9. Agricultural sales should show some improvement over the previous year. Although irrigated cotton acreage is expected to remain unchanged from 1974, dry-farm crops will probably exceed the previous year's harvest because of improved moisture conditions.

10. Damascus has placed a high priority on the development of phosphate deposits. Transportation difficulties, which previously hampered growth, will be largely eliminated by the current extension of the railway system. Production in 1975 is projected at 1.2 million metric tons, more than twice the 1974 level. Nevertheless, falling world prices for phosphate fertilizers coupled with increased domestic consumption could result in lower than anticipated export earnings from fertilizer.

Imports

11. Syrian imports should expand 45% this year. Prices are expected to increase 12% and real volume, 29%.

12. Major defense purchases are not included in this estimate. Despite acquisition of more than \$1 billion worth of military equipment from the Soviet Union over the past two years, Syria has no pressing repayment burden. Long-term credit agreements with extended grace period provisions cover all major hardware purchases. Even if the Soviets tighten payment schedules for political reasons, Damascus would be unlikely to suffer, because Arab benefactors would quickly provide the necessary assistance.

13. A major increase in foodstuff imports in 1974 followed the poor agricultural performance in 1973, when output dropped to one-third the normal

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level. Food imports have largely returned to normal after adequate rainfall in 1974 and early 1975. We expect food purchases to decline about 30% below last year's level.

14. Development projects will absorb by far the greatest share of Syrian imports. The government planning agency projects overall spending to exceed \$1.5 billion. Most funds are earmarked for such capital-intensive projects as new textile mills, fertilizer plants, a new refinery, and other petroleum-related facilities. Total development imports will probably be about \$1 billion. Greater import volumes for development projects are unlikely during 1975. Port facilities are already seriously congested, and the current shortage of skilled labor may become more acute as the year progresses.

15. Consumer import requirements may increase by 50% in 1975 to a level of \$150 million. The Assad regime previously restricted consumer imports in the name of the struggle against Israel. However, a relaxation of tensions in the area combined with greatly improved economic conditions will probably lead to an easing in restrictions.

Net Services and Private Transfers

16. Earnings from net services will decline \$15 million during 1975, largely from a dip in oil transit earnings. Private transfer payments, on the other hand, should reflect growing remittances from Syrian residents abroad, chiefly in Lebanon and the Gulf states. Although Damascus is attempting to discourage a further exodus of workers, higher wage rates in the Gulf and Lebanon provide an irresistible pull. Projected private transfers amount to \$56 million, a 40% increase over the 1974 level.

Financing the Deficit

Grant-Type Assistance

17. Grant-type assistance payments during 1975 will reach \$730 million, 60% greater than the previous year's level. Arab "Rabat" payments to Syria of \$580 million dominate these transfers. Saudi Arabia increased its subscription by \$150 million to meet the costs of war reconstruction.

Other Capital Inflows

18. We believe that private capital flows will remain sluggish throughout most of the year, with total spending rising \$10 million or so above last year's \$15 million level. Unsettled political conditions in the area are causing many firms, including independent US oil companies, to postpone major investment decisions during 1975. The slow growth of private capital inflows also stems from a continuing Syrian reluctance to accept large-scale direct investment. Although the Assad regime is now discussing new incentives to private companies, the government still prefers direct control over all projects, with foreign companies limited to providing expertise on a contract basis. Although this attitude may shift as economic development progresses, the volume of private capital inflows is unlikely to grow sharply during the current year.

19. Conversely, development flows from official sources are scheduled to expand greatly in 1975. The Saudis are providing a 3-year, \$220 million development loan. Development aid from all other sources is now set at approximately \$183 million.

Medium-Term Development Outlook

20. Medium-term economic development prospects are encouraging, the major uncertainty being outbreak of large-scale conflict in the Middle East. Israeli bombing could once again produce a devastating short-term impact on the economy, particularly in the petroleum and the electrical power generating sectors.

21. Barring renewal of major fighting, economic conditions should remain favorable. There are indications that Syria's proved oil reserves will be increased over the next several years - perhaps tripling the current 7 billion barrel figure. In March, Damascus signed an agreement with a group of independent US oil companies for offshore exploration on Syria's Mediterranean coast. Other US companies are presently negotiating for similar agreements.

22. Plans to develop a major food industry, based on domestic agriculture and directed toward local consumption and export, appear well founded. Inefficient traditional farming methods, lack of agricultural planning, and the aftereffects of a decade of land reform depressed agricultural output until recently. However, the potential for agricultural expansion exists in terms of both abundant fertile land and excellent water resources. The impact of the new Euphrates dam project at

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Tabagah will be enormous.* Waters from the new project will double the amount of irrigated land available for agricultural development. Better agricultural organization, methods, and planning as well as the increased availability of domestically produced fertilizers should lead to far greater agricultural output in the future. Improvements in the transportation network will also enhance development prospects in this crucial sector.

23. The hydroelectric development associated with the Euphrates dam will double Syrian electric generating capacity and provide relatively cheap electricity for industrial development. Among the industries slated for rapid expansion is cement; its current capacity of about one million tons is to be doubled by 1980. Substantial capacity increases are also planned for sugar refining and textiles.

24. Damascus remains committed to a policy of rapid economic development with or without movement toward peace in the Middle East. While economic benefits of reduced tensions appear enticing, so long as Arab aid continues at its current level the Assad government is unlikely to compromise its political goals for the sake of any economic considerations.

25. Reduced tensions in the area would ease an acute shortage of skilled and semiskilled labor by releasing workers from defense-related requirements. The Syrian labor squeeze, already serious, is likely to worsen as more development projects move to site preparation and "bricks and mortar" activity. Although the labor supply could be imported from the Palestinian camps and from Egypt in the near term, there is a high political resistance to such a move.

26. A negotiated settlement in the Middle East that did not compromise Syria's political relations with Arab aid donors could substantially improve economic prospects. Private foreign investors, including American firms, remain reluctant to undertake major projects in Syria so long as political conditions in the region are unsettled.

* Lake Assad, the reservoir created by the dam, should reach full capacity late this year, unless Iraqi political pressure forces a slowdown in reservoir buildup.

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